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No. 70

In the

# Supreme Court of the United States

October Term 1949

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JOHN E. MANNING, as Collector of Internal Revenue for the Fifth District of New Jersey,

vs.

SEELEY TUBE AND BOX COMPANY, a Corporation of the State of New Jersey.

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**BRIEF ON BEHALF OF**

**GORDEN F. DeFOSSET**
1104-10 B. F. Keith Bldg.,
Cincinnati 2, Ohio.

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**AMICUS CURIAE.**

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## AMICUS CURIAE.

## OPINION BELOW

The opinion of the District Court is reported in 76 Federal Supp. 937. The opinion of the Court of Appeals is reported in 172 Federal 2nd. 77.

## QUESTION PRESENTED

The question before the court is whether a taxpayer who suffers a net operating loss in 1943 and pursuant to the Internal Revenue Code carries said loss back to 1941 and is thereby entitled to a refund, shall have that refund reduced by the Commissioner in the amount of interest computed on additional taxes found to be due for 1941. Or put more directly: If the Government owes the taxpayer a refund and the taxpayer owes the Government a tax liability less than the amount of the refund, both for the same year, is the Government entitled to assess interest on the liability the taxpayer owes the Government.

## STATEMENT

The answer to the problem above stated may only be found in the Internal Revenue Code. All matters involving the relationship between the taxpayer and his government must be solved by an interpretation of the statutes and the decided cases, for income taxation is wholly statuatory.

With the exception of the lower court opinions in this case and the case of *Brandtjen and Kluge, Inc.* v. *United States*, 78 Federal Supp. 509 (D. Minn.) there is no case law dealing directly with this problem. Therefore the only solution must be found in the pertinent statutes and their logical interpretation.

## I

If the Commissioner is to charge the taxpayer interest he must do so as the result of Sec. 292 (a) of the Internal Revenue Code (26 U. S. C. 292).

Sec. 292. INTEREST ON DEFICIENCIES.

(a) (As amended by Sec. 2 (a) of the Act of December 17, 1943, c 346, 57 Stat. 601). General Rule.—Interest upon the amount determined as a deficiency shall be assessed at the same time as the deficiency, shall be paid upon notice and demand from the collector, and shall be collected as a part of the tax, at the rate of 6 per centum per annum from the date prescribed for the payment of the tax (or, if the tax is paid in installments, from the date prescribed for the payment of the first installment) to the date the deficiency is assessed * * * *.

The real meaning of this section cannot be ascertained until we know what a deficiency is. This is defined by Section 271 (26 U. S. C. 271).

SEC. 271. DEFINITION OF DEFICIENCY.

As used in this chapter in respect of a tax imposed by this chapter "deficiency" means—

(a) The amount by which the tax imposed by this chapter exceeds the amount shown as the tax by the taxpayer upon his return; but the amount so shown on the return shall first be increased by the amounts previously assessed (or collected without assessment) as a deficiency, and decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax; or

(b) If no amount is shown as the tax by the taxpayer upon his return, or if no return is made by the taxpayer, then the amount by which the tax exceeds the amounts previously assessed (or collected without assessment) as a deficiency; but such amounts previously

assessed, or collected without assessment, shall first be decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax.

Stripped of its verbage it defines a deficiency as the difference between the tax shown on the original return plus any additional tax assessed, less any amount abated, credited, refunded or otherwise repayed because the amount due was less than that which was found to be due.

Therefore when by reason of a carry back the taxpayer is entitled to a refund for 1941 in excess of the amount of tax shown on the return plus any amount previously assessed for the year in question (1941) there can be by the very definition of a deficiency no deficiency and consequently no interest.

The Commissioner realizes that no deficiency exists in a case such as is before this court for he refers to the foundation on which he would charge interest as a "potential deficiency." One may search the Code minutely and never find a definition of such a term. There is no possible way to have a "potential deficiency" under the Internal Revenue Code.

II.

If there is no deficiency but instead an overpayment then following the code it appears at Sec. 322(a) (26 U. S. C. 322) the method by which an overpayment is to be handled.

SEC. 322. REFUNDS AND CREDITS.

(a) Authorization.—

(1) Overpayment.—Where there has been an overpayment of any tax imposed by this chap-

> ter, the amount of such overpayment shall be credited against any income, war-profits, or excess-profits *tax* or installment thereof then due from the taxpayer, and any balance shall be refunded immediately to the taxpayer.

It is important to note that this section specifically holds that any overpayment *shall* be credited against any *tax* due and the balance refunded immediately to the taxpayer.

This Court has held in (*U. S.* v. *Childs* 266 U. S. 304, 45 S. Ct. 110) that interest while it is collected as part of the tax is not a tax.

Therefore when the Commissioner finds that there is an overpayment such as he did in this instance may he in direct contravention of the mandatory language of Sec. 322 credit a part of that overpayment to interest.

The case of *Brandtjen & Kluge, Inc.*, v. *U. S. Supra*, interprets Sec. 322 in exactly this manner. In that case the taxpayer paid its deficiency plus interest only to find out later by reason of a carry back it was entitled to the original tax plus the deficiency on a refund. The Commissioner issued the refund but refused to return the interest previously collected. The Court in holding for the Government said that since interest is not a tax and Sec. 322 says "where there has been an overpayment of any *tax* etc." then the Commissioner may not refund the interest because this section only requires him to refund the tax. If the first sentence of Sec. 322 is to be interpreted strictly then certainly the balance of the section should receive the same interpretation.

The Commissioner might conceivably argue that Sec. 3771 (e) 26 U. S. C. 3771 requires him to charge interest on what the Bureau calls a "potential deficiency." This

conclusion certainly does not follow if one examines that section closely. All that Sec. 3771 means is that the taxpayer is not entitled to interest on any refund due to a carry back prior to filing his claim for a refund. In the instant case the taxpayer is not asking for interest on the amount due on the refund but instead is asking that the Commissioner not charge interest on an inchoate liability.

## III.

If this problem is to be finally determined by this Court for the efficient administration of the Bureau of Internal Revenue and certainly for the taxpayers, it might be valuable to assume a set of facts somewhat different than the case at Bar.

Assuming that the taxpayer does not agree to a waiver of the restrictions on assessment as he has the right to do under Sec. 272(d). Then pursuant to paragraph (a) and (b) of said section the Commissioner may not assess a deficiency until either 90 days has elapsed after sending taxpayer his proposed assessment or until, if the taxpayer has filed a petition with the Tax Court, that Court's decision becomes final.

Therefore if the taxpayer after receiving the 90 day notice files a Petition with the tax court for the year out of which the proposed deficiency arises he may set up in that proceeding the carry back from a subsequent year. Sec. 272 (g), *Birch Ranch & Oil Co.* 48039 Prentice Hall Memo. T. C., 17 T. C. Memo. Dec. 132. If this carry back is large enough to eliminate the proposed deficiency (as in the case at bar) then the Tax Court must find that no deficiency exists and will find that an overpayment exists.

Should the Commissioner attempt to assess this proposed deficiency prior to the time stated in Sec. 272(a) he may be enjoined by a proper proceeding as stated in Sec. 272(a) (1).

It follows logically that if the Tax Court determines that no deficiency exists there may then be no interest collected.

While the above situation admittedly presents a different set of facts than is here in the case at bar it can easily be seen that a decision in favor of the Commissioner in the instant case would force taxpayers to resort to the procedure outlined in the assumed case above with the consequent crowding of the Tax Court's dockets, a tribunal that is even now overburdened with litigation. The procedure before the Tax Court would of necessity be only a formality since in almost all of this type of cases the taxpayer and the Commissioner are in agreement as to the amount of the carry back as well as the amount of the additional tax proposed. Requiring taxpayer as well as the Commissioner, to resort to this added expense and time would certainly be a result not in the best interest of either party or the intention of Congress.

## CONCLUSION

The Commissioner is in error when he charges the taxpayer's refund with interest computed on a potential deficiency for the following reasons:

1: There is no deficiency and therefore there can be no interest. Subdivision I supra.

2: His procedure in making such charge is in contravention of the mandatory language of the code concerning the handling of overpayments. Subdivision II Supra.

3: To conclude this problem in favor of the Commissioner would force taxpayers as well as the Commissioner into the Tax Court for a mere formality (Subdivision III Supra).

The answer to the problem presented here to the Court can best be stated in the homey, common sense language of the Court below "Interest on nothing (what the taxpayer owed the government) is necessarily nothing."

Respectfully submitted.

Gorden F. DeFosset,
1104-1110 B. F. Keith Bldg.,
Cincinnati 2, Ohio.

# APPENDIX

## Internal Revenue Code.

Sec. 271. DEFINITION OF DEFICIENCY.

As used in this chapter in respect of a tax imposed by this chapter "deficiency" means—

(a) The amount by which the tax imposed by this chapter exceeds the amount shown as the tax by the taxpayer upon his return; but the amount so shown on the return shall first be increased by the amounts previously assessed (or collected without assessment) as a deficiency, and decreased by the amount previously abated, credited, refunded, or otherwise repaid in respect of such tax; or

(b) If no amount is shown as the tax by the taxpayer upon his return, or if no return is made by the taxpayer, then the amount by which the tax exceeds the amounts previously assessed (or collected without assessment) as a deficiency; but such amounts previously assessed, or collected without assessment, shall first be decreased by the amounts previously abated, credited, refunded or otherwise repaid in respect of such tax. (26 U. S. C. 271.)

Sec. 272. PROCEDURE IN GENERAL.

(a) (1) Petition to Board of Tax Appeals. If in the case of any taxpayer, the Commissioner determines that there is a deficiency in respect of the tax imposed by this chapter, the Commissioner is authorized to send notice of such deficiency to the taxpayer by registered mail.

Within ninety days after such notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the ninetieth day), the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the deficiency. No assessment of a deficiency in respect of the tax imposed by this chapter and no distraint or proceeding in Court for its collection shall be made, begun, or prosecuted until such notice has been mailed to the taxpayer, nor until the expiration of such ninety-day period, nor, if a petition has been filed with the Board, until the decision of the Board has become final. Notwithstanding the provisions of Section 3653(a) the making of such assessment or the beginning of such proceeding or distraint during the time such prohibition is in force may be enjoined by a proceeding in the proper court. In the case of a joint return filed by husband and wife such notice of deficiency may be a single joint notice, except that if the Commissioner has been notified by either spouse that separate residences have been established, then, in lieu of the single joint notice, duplicate originals of the joint notice must be sent by registered mail to each spouse at his last known address. If the notice is addressed to a person outside the States of the Union and the District of Columbia, the period specified in this paragraph shall be one hundred and fifty days in lieu of ninety days.

(b) Collection of Deficiency Found by Board.—If the taxpayer files a petition with the Board, the entire amount redetermined as the deficiency by the decision of the Board which has become final shall be assessed and shall be paid upon notice and demand from the collector. No part of the amount determined as

a deficiency by the Commissioner but disallowed as such by the decision of the Board which has become final shall be assessed or be collected by distraint or by proceeding in court with or without assessment.

(c) Failure to File Petition.—If the taxpayer does not file a petition with the Board within the time prescribed in subsection (a) of this section, the deficiency, notice of which has been mailed to the taxpayer, shall be assessed, and shall be paid upon notice and demand from the collector.

(d) Waiver of Restrictions.—The taxpayer shall at any time have the right, by a signed notice in writing filed with the Commissioner, to waive the restrictions provided in subsection (a) of this section on the assessment and collection of the whole or any part of the deficiency.

(g) Jurisdiction Over Other Taxable Years.—The Board in redetermining a deficiency in respect of any taxable year shall consider such facts with relation to the taxes for other taxable years as may be necessary correctly to redetermine the amount of such deficiency, but in so doing shall have no jurisdiction to determine whether or not the tax for any other taxable year has been overpaid or underpaid. (26 U. S. C. 272.)

Sec. 292. INTEREST ON DEFICIENCIES.

(a) (As amended by Sec. 2(a) of the Act of December 17, 1943, c 346, 57 Stat. 601.

General Rule.—Interest upon the amount determined as a deficiency shall be assessed at the same time as the deficiency, shall be paid upon notice and demand from the collector,

and shall be collected as a part of the tax, at the rate of 6 per centum per annum from the date prescribed for the payment of the tax (or, if the tax is paid in installments, from the date prescribed for the payment of the first installment) to the date the deficiency is assessed * * * *. (26 U. S. C. 292.)

Sec. 322. REFUNDS and CREDITS.

(a) Authorization.—

(1) Overpayment.—Where there has been an overpayment of any tax imposed by this chapter, the amount of such overpayment shall be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance shall be refunded immediately to the taxpayer. (26 U. S. C. 322.)

Sec. 3771. INTEREST ON OVERPAYMENTS.

(a) Rate.—Interest shall be allowed and paid upon any overpayment in respect of any internal revenue tax at the rate of 6 per centum per annum.

(b) Period.—Such interest shall be allowed and paid as follows:

(c) (As added by Sec. 153(d) of the Revenue Act of 1942, supra). Claims Based on Carry-Back of Loss or Credit.—If the Commissioner determines that any part of an overpayment is attributable to the inclusion in computing the net operating loss deduction for the taxable year of any part of the net operating loss for a succeeding taxable year or to the inclusion in computing the unused excess profits credit adjustment for the taxable year of any part of the

unused excess profits credit for a succeeding taxable year, no interest shall be allowed or paid with respect to such part of the over payment for any period before the filing of a claim for credit or refund of such part of the overpayment or the filing of a petition with the Board, whichever is earlier. (Sec. U. S. C. 3771.)